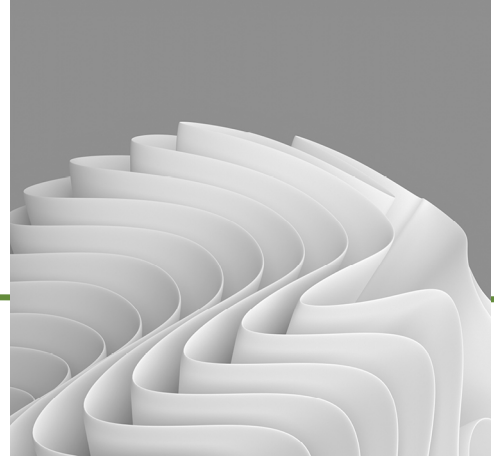


# MARKET SIGHT LINES



## Spotlight No. 3: Outlook 2024: *Embracing Change* Our Scenarios

By Michael O'Keeffe, *Chief Investment Officer*



As we've been discussing, my team and I released our outlook report, *Outlook 2024: Embracing Change* earlier this month, including a [full report](#), [video summary](#), and [client webinar replay](#), as well as a [summary of our report](#) and [a summary of our outlook](#). In this week's Sight|Lines, we explain our bear and bull scenarios included in our outlook report.

### **THE TAKEAWAY: THE BEAR AND BULL SCENARIOS MAY HAPPEN, BUT WE HOPE NOT**

Each year our outlook includes three scenarios: a base case, a bear case, and a bull case. This year, we anchor our framework on three things: the consumer, earnings, and animal spirits. In summary:

- As we discussed [last week](#), our base case is for a less active consumer but positive economy and positive earnings growth below consensus, leading to a modestly positive stock market and animal spirits that are little changed.
- In our bear case, perhaps triggered by the pain of higher rates or an unknown catalyst like another geopolitical hotspot, the consumer slows spending more significantly, negatively impacting earnings and stocks, further amplified by weakened animal spirits.
- In our bull case, the consumer ignores the negatives and continues spending unchecked, fueling stronger earnings, improving animal spirits, and a likely double-digit stock market return.
- We're not fans of our bull case, as irrational spending by the consumer may lead to more debt, which builds up our [Fiscal Transition](#) problems down the road.
- We see the chances for the bull and bear cases to be higher than normal.

### **IN-DEPTH: ANCHORED ON THE CONSUMER, EARNINGS, AND ANIMAL SPIRITS, OUR ALTERNATE SCENARIOS HAVE FAT TAILS AGAIN, EACH NEGATIVE IN ITS OWN WAY**

This year we again framed up three scenarios: our base case, bear case, and bull case. Going deeper:

- We anchored our framework on three important components:
  - The consumer, which drives about two-thirds of economic activity
  - Earnings, which drive stock performance
  - Animal spirits, the emotions and instincts influencing economies and markets
- [Last week](#), we reviewed our base case:
  - We see a less active consumer muting still positive economic growth.

- We expect positive earnings growth and stocks to produce muted positive returns.
- Animal spirits remain stable, in line with last year.
- Our bear case may or may not be initiated by an unknown event, like a new geopolitical hotspot:
  - A worried consumer would slow her/his spending much more significantly.
  - A less active consumer, and related muted business activity, would erode earnings.
  - Weakened animal spirits would exacerbate the problem, leading to a market correction (defined as down 10%) or a bear market (defined as down 20%).
- Our bull case anchors on the idea that, despite problems, the consumer keeps spending.
  - In this scenario, the consumer ignores the negatives and “spends beyond their means.”
  - A more active consumer, and related stronger business activity, would expand earnings.
  - A happy consumer, and better business, would drive even more positive animal spirits, likely leading to a double-digit stock market return for the year.
- Each year we assign a probability to each scenario as a way to anticipate, and try to plan for, the chances of each scenario actually happening. For 2024:
  - We assign our base case, which we view as modestly positive, a probability of 55%, making it the most likely scenario, in our view.
  - We assign our bull case, which is much more positive, a 20% probability.
  - Finally, we see a 25% probability of our bear case, so a chance for this negative scenario.
  - The “tail” probabilities, 20% and 25%, are higher than normal, what are called “fat tails.”
- Through 2023, and in our [outlook report](#), we discussed the challenges of *Fiscal Transition*, or the idea that increased debt and higher rates spell trouble:
  - So, while we normally hope that our bull case unfolds, this year we don’t.
  - A consumer “spending beyond their means” fuels more debt, delaying the positive benefits of going through a [Fiscal Transition](#).

## CONCLUSION

To start the year, my team and I released **Outlook 2024: Embracing Change** with a [full report](#), [video summary](#), and [client webinar replay](#). As has been our practice, we included a discussion of three scenarios: our base case, bear case, and bull case views. By working through various possibilities, we’re more ready, and even excited, for what’s in store in 2024.

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